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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION THREE

ORTHOLA, INC. et al., Plaintiffs and Respondents, v. DEPUY SYNTHES SALES, INC., Defendant and Appellant.	B296589 (Los Angeles County Super. Ct. No. 18STCV02833)

APPEAL from an order of the Superior Court of Los Angeles County, Rafael A. Ongkeko, Judge. Reversed.

Blank Rome, Gregory M. Bordo, Cheryl Chang and Anthony B. Haller for Defendant and Appellant.

Julander Brown & Bollard, Dirk O. Julander, M. Adam Tate, Tiffany Wang; Ostergar Law Group and Treg A. Julander for Plaintiffs and Respondents.

DePuy Synthes Sales, Inc. (DePuy) appeals from the trial court's order denying its motion to compel OrthoLA, Inc. (OrthoLA) and Bruce Cavarno's claims to arbitration. DePuy contends the trial court should have sent the threshold issue of whether there was an enforceable agreement to arbitrate to the arbitrator and then erred again when it found the agreements unconscionable and thus unenforceable. We agree and reverse the order.

BACKGROUND

DePuy designs, manufactures, and sells medical implants and instruments used in orthopedic surgeries and is based in Warsaw, Indiana. It is one of the largest medical device companies in the world and has gross revenues in the United States of over $2 billion. OrthoLA was a distributor of DePuy's medical devices in the Los Angeles area and had gross revenues of approximately $50 million at the end of 2017. Cavarno is OrthoLA's founder and principal.

DePuy and OrthoLA's distribution relationship was governed by the sales representative agreement (SRA), which authorized OrthoLA to act as a sales representative of DePuy's products in and around the Los Angeles area. Additionally, DePuy and OrthoLA entered into a supplemental agreement, the continuing income agreement (CIA), which was intended to be the functional equivalent of a pension for Cavarno. Under the CIA, DePuy agreed to pay Cavarno for a period of 10 years after the termination of the parties' distribution relationship so long as OrthoLA did not compete with DePuy. As a condition of payment under the CIA, Cavarno was required to comply with section 4.4 of the SRA, which prohibited him or OrthoLA from engaging in "Solicitation Activities" during the parties' relationship and for a period of one year thereafter. Section 4.4 reads in part: "Solicitation Activities

shall mean to, whether directly or indirectly, solicit, employ or offer to employ, retain or offer to retain (whether as an independent contractor or otherwise), any (i) employee, contractor or agent of [DePuy], or (ii) any person or entity which is engaged, whether full-time or part-time, as an employee, contractor or agent of any third party in the marketing, sale or distribution of any Product or any other products or services of DePuy."

During the negotiations of the SRA and CIA, the parties each had their own separate counsel. Cavarno stated that he and his attorney "pressed very hard to get DePuy to eliminate the non-competition language of section 4.4" of the SRA, but DePuy refused. However, DePuy agreed to add a provision that section 4.4 would not apply if it was found unenforceable under California law. Thus, while the remainder of the contract was to be governed by Indiana law, under section 4.4, California law controlled.

Both the SRA and CIA contain arbitration provisions. Section 14.1 of the SRA and section 7.1 of CIA read: "Any controversy or claim arising out of or relating to this Agreement shall be resolved by arbitration before a single arbitrator in accordance with the Commercial Arbitration Rules of American Arbitration Association ('AAA') then pertaining (available at www.adr.org), except where those rules conflict with this provision, in which case this provision controls. Any court with jurisdiction shall enforce this clause and enter judgment on any award." (Italics omitted.) Under the agreements, an arbitrator or a court of competent jurisdiction could sever any provision that is invalid or unenforceable.

Eventually the relationship between the parties soured and OrthoLA sued DePuy for intentional interference with contractual relationships, intentional and negligent interference with

prospective economic advantage, unfair competition, breach of the CIA, breach of the covenant of good faith and fair dealing, and declaratory relief. The declaratory relief cause of action sought an order declaring unenforceable section 4.4 of the SRA and those terms of the CIA that conditioned payment on compliance with section 4.4 because they violated California's fundamental public policy against restraints on trade. The declaratory relief cause of action also sought to invalidate the agreements' arbitration provisions.

DePuy moved to compel OrthoLA's claims to arbitration, asserting the arbitration provisions should be enforced according to the Federal Arbitration Act (9 U.S.C. § 1 et seq.; hereafter FAA), that California and Indiana law favored arbitration, and that neither agreement was unconscionable because they were the result of negotiations by sophisticated parties through their respective counsel.

OrthoLA responded that the arbitration provisions were unconscionable because the SRA and CIA were presented on a take-it-or-leave-it basis, contained unilateral obligations to arbitrate, were drafted to circumvent California law, and selected a forum that was unrelated to the parties' transactions or locations. With respect to the first version of the SRA, Cavarno stated that, when it was first presented to him and his lawyer, he was told he "had to sign the contract or no deal." Cavarno also said he felt compelled to agree to the CIA's terms to keep his pension following his work with DePuy. Further, he believed there was "no legitimate reason" why the dispute should be litigated in Indiana rather than California because he was a California resident, OrthoLA was a California corporation, and the majority of witnesses were located in California.

The trial court denied DePuy's motion. It first determined that California law should apply, finding that applying Indiana law would contravene California's public policy against covenants not to compete. It then concluded that the arbitration provisions were both procedurally and substantively unconscionable. The trial court found the amount of procedural unconscionability was "slight" because, even though the agreements were prepared and negotiated by both parties' counsel, there was an obvious disparity in the parties' relative economic bargaining power and respective roles in the relevant market. In contrast, the trial court found a "high degree of substantive unconscionability" because the agreements: (1) contained unilateral obligations to arbitrate in favor of DePuy, (2) required the application of Indiana law in circumvention of California's public policy against non-compete agreements, and (3) required the parties to arbitrate in Indiana.

DISCUSSION

We review an appeal from an order denying a motion to compel arbitration de novo. (*Baker v. Osborne Development Corp.* (2008) 159 Cal.App.4th 884, 892.) To the extent the trial court's determination turned on the resolution of contested facts, we review the factual determinations for substantial evidence. (*Ibid.*)

According to the arbitration provisions, their interpretation and enforcement is governed by the FAA. When a party seeks to enforce an arbitration agreement within the FAA's scope, courts apply state contract law while showing deference to the federal policy favoring arbitration. (*Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University* (1989) 489 U.S. 468, 474.)

DePuy raises several arguments in support of reversal. However, we find only two relevant here, whether the parties

delegated threshold questions to the arbitrator and whether the trial court erred when it found the arbitration provisions unconscionable and thus unenforceable. For the reasons stated below, we find that the trial court was the proper decision maker, but it erred when it concluded that the agreements were procedurally unconscionable.

I. The SRA and CIA do not clearly and unmistakably delegate enforceability to the arbitrator and, in any event, the issue was waived.

DePuy's first contention is that the trial court failed to enforce the delegation clauses contained within the arbitration provisions. In other words, the trial court had no authority to decide the threshold question of whether the arbitration agreements were enforceable because the parties agreed that only the arbitrator could decide that issue. We disagree.

The FAA allows parties to agree by contract that an arbitrator, rather than a court, can resolve threshold arbitrability questions, such as enforceability. (*Rent-A-Center, West, Inc. v. Jackson* (2010) 561 U.S. 63, 68–70.) Thus, the parties can have the arbitrator not only decide the merits of a dispute but also gateway questions of arbitrability, such as the existence of a valid and enforceable arbitration agreement or whether the parties agreed to arbitrate a particular controversy. (*Henry Schein, Inc. v. Archer and White Sales, Inc.* (2019) ___ U.S. ___, ___ [139 S.Ct. 524, 529].) This delegation of authority must be clear and unmistakable, otherwise the trial court retains jurisdiction over those threshold determinations. (*AT&T Technologies v. Communications Workers* (1986) 475 U.S. 643, 649.) "In this manner the law treats silence or ambiguity about the question [of] 'who (primarily) should decide arbitrability' differently from the way it treats silence or ambiguity

about the question 'whether a particular merits-related dispute is arbitrable because it is within the scope of a valid arbitration agreement'—for in respect to this latter question the law reverses the presumption." (*First Options of Chicago, Inc. v. Kaplan* (1995) 514 U.S. 938, 944–945.) Without clear and unmistakable evidence that the parties gave the arbitrator the power to decide the enforceability of the agreement or arbitrability of an issue, the trial court is the proper decision maker. (*Id.* at p. 945.)

DePuy argues for the first time on appeal that the SRA and CIA contain delegation clauses and that the trial court should have sent the issue of enforceability to the arbitrator. This contention fails twofold. First and foremost, DePuy never raised this contention below and the failure to raise an issue or argument in the trial court waives the point on appeal.[1] (See *Kolani v. Gluska* (1998) 64 Cal.App.4th 402, 411.) Second, even if the contention was not waived, neither the SRA nor the CIA contains clear and unmistakable evidence that the parties intended for an arbitrator to have exclusive jurisdiction over whether the arbitration agreements were enforceable. To the extent the agreements contain delegation provisions, they are ambiguous. For example, both arbitration provisions state that any controversy or claim arising out of or relating to those agreements shall be resolved by arbitration before a single arbitrator, however, the same provisions go on to state that

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[1] Notably, the case that DePuy now contends should control, *Rent-A-Center, West, Inc. v. Jackson*, *supra*, 561 U.S. 63, was not cited in its motion or reply papers. In fact, DePuy tried to partially distinguish another case, *Pinela v. Neiman Marcus Group, Inc.* (2015) 238 Cal.App.4th 227, on the grounds that it addressed a delegation clause in an arbitration agreement, asserting, no "such facts are present here."

any "court with jurisdiction shall enforce this clause." Moreover, the agreements' severability clauses contemplate that either a court of competent jurisdiction or an arbitrator may sever invalid or unenforceable provisions to preserve the remainder of the agreements. Each of these terms creates an ambiguity, suggesting that either an arbitrator or a court can determine enforceability.[2]

Because the arbitration provisions in both the SRA and CIA were ambiguous on the question of who should decide enforceability, the trial court was the proper decision maker here. (See *First Options of Chicago, Inc. v. Kaplan*, *supra*, 514 U.S. at p. 944.) This conclusion is consistent with other cases interpreting arbitration agreements containing similar ambiguous delegation and severability clauses. (See, e.g., *Parada v. Superior Court* (2009) 176 Cal.App.4th 1554, 1566 [term "trier of fact of competent jurisdiction" suggests trial court may decide enforceability of arbitration provision]; *Hartley v. Superior Court* (2011) 196 Cal.App.4th 1249, 1257–1258 [same]; see *Peleg v. Neiman Marcus Group, Inc.* (2012) 204 Cal.App.4th 1425, 1444.)

II. The SRA and CIA were not unconscionable.

While we disagree with DePuy's argument that the trial court should have sent the threshold issue of enforceability to the

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[2] The SRA and CIA's incorporation of the Commercial Arbitration Rules of the American Arbitration Association does not clarify this ambiguity. Those rules state that, the "arbitrator shall have the power to rule on his or her own jurisdiction, including any objections with respect to the existence, scope, or validity of the arbitration agreement or to the arbitrability of any claim." Thus, while the arbitrator has the power to decide his or her jurisdiction, the incorporated rules do not make that authority exclusive.

arbitrator, we agree with DePuy that the agreements were not procedurally unconscionable.

" '[G]enerally applicable contract defenses, such as . . . unconscionability, may be applied to invalidate arbitration agreements without contravening' the FAA." (*Pinnacle Museum Tower Assn. v. Pinnacle Market Development (US), LLC* (2012) 55 Cal.4th 223, 246.) An unconscionability defense consists of both procedural and substantive elements. (*Ibid.*) "The procedural element addresses the circumstances of contract negotiation and formation, focusing on oppression or surprise due to unequal bargaining power. [Citations.] Substantive unconscionability pertains to the fairness of an agreement's actual terms and to assessments of whether they are overly harsh or one-sided." (*Ibid.*) Both procedural and substantive unconscionability must be shown, however, they need not be present in the same degree and are evaluated on a sliding scale. (*Id.* at p. 247.) The " 'more substantively oppressive the contract term, the less evidence of procedural unconscionability is required to come to the conclusion that the term is unenforceable, and vice versa.' " (*Ibid.*)

Procedural unconscionability concerns the manner in which the contract was negotiated and the circumstances of the parties at the time. We look to whether oppression played a role in the execution of the agreement and whether a party was surprised by the presence of hidden terms. (*Pinnacle Museum Tower Assn. v. Pinnacle Market Development (US), LLC*, *supra,* 55 Cal.4th at p. 246.) " ' " 'Oppression occurs where a contract involves lack of negotiation and meaningful choice, surprise where the allegedly unconscionable provision is hidden within a prolix printed form.' " ' " (*Magno v. The College Network, Inc.* (2016) 1 Cal.App.5th 277, 285.) There " 'are degrees of procedural unconscionability. At

one end of the spectrum are contracts that have been freely negotiated by roughly equal parties, in which there is no procedural unconscionability. . . . Contracts of adhesion that involve surprise or other sharp practices lie on the other end of the spectrum.' " (*Baltazar v. Forever 21, Inc.* (2016) 62 Cal.4th 1237, 1244.)

Neither oppression nor surprise is present here. The SRA and CIA were prepared and negotiated by both parties' counsel. As one of the largest medical device suppliers in the world, it is undisputed that DePuy was in a superior economic bargaining position. However, OrthoLA was still able to negotiate a favorable term of the SRA. Specifically, DePuy agreed that the noncompetition language of section 4.4 of the SRA would not apply if its non-compete clause was unenforceable under California law. The parties dispute the significance of this fact. On one hand, DePuy contends this is evidence of a "real negotiation" between the parties. On the other, OrthoLA asserts that it highlights the disparity in bargaining power between the parties because it was the only modification DePuy accepted over the parties' nine-year distribution relationship and the modification did not constitute a substantive change to the terms of the SRA.

OrthoLA's characterization, however, is undermined both by the terms of the SRA and its contention that the agreements are substantively unconscionable because they require the application of Indiana law. For example, despite section 4.3 of the SRA's restriction on the sale of competitive products, section 4.5 acknowledges that Cavarno is already an independent sales contractor for other medical device companies and that he may continue to sell those products from those companies listed. Thus, there is at least one modification that Cavarno was able to secure to a contract he now contends was presented to him on a take-it-or-

leave-it basis. Further, OrthoLA's attempt to minimize the significance of the modification to section 4.4 is contrary to its primary contention that the agreements are substantively unconscionable because they require the application of Indiana law and allow DePuy to thwart California's public policy against noncompetition agreements. Either the application of California law is of significant import to OrthoLA or it is not.

Further, not only were both parties represented by counsel who negotiated substantive terms of the agreements, each are sophisticated business entities. DePuy had gross revenues in the United States of over $2 billion and is a part of the Johnson & Johnson family of companies. Although comparatively small in gross revenue, OrthoLA was one of four distributors in the joint replacement industry that controlled 90 percent of the market in the Los Angeles area. To the extent the trial court's finding of procedural unconscionability was based on the complaint's detailed allegations of the "fiercely competitive medical sales industry in Los Angeles County," those allegations are not evidence for purposes of considering a motion to compel arbitration. (See *Hotels Nevada v. L.A. Pacific Center, Inc.* (2006) 144 Cal.App.4th 754, 761–762.)

Relying on *Bakersfield College v. California Community College Athletic Assn.* (2019) 41 Cal.App.5th 753, OrthoLA asserts that, just because both parties to an arbitration agreement are sophisticated does not necessarily mean procedural unconscionability is absent. In *Bakersfield*, the court found an arbitration agreement between an intercollegiate athletic association and a college was procedurally unconscionable even though both parties were sophisticated entities. (*Id.* at pp. 757, 764.) The arbitration agreement was contained in the athletic association's constitution and bylaws, which the court construed as

a standardized contract that the college had to accept or forfeit its right to participate in intercollegiate athletic competitions. (*Id.* at p. 763.) The *Bakersfield* court found that even though both parties were sophisticated, this did not alter the contract as one of adhesion when the college had no opportunity to negotiate changes to the agreement via proposed amendments to the constitution and bylaws once it agreed to the athletic association's terms. (*Id.* at pp. 763–764.) *Bakersfield* is distinguishable in that, as discussed above, OrthoLA was able to negotiate a modification to section 4.4 of the SRA that also bore directly on the CIA, as that latter agreement conditioned the continuing income payments to Cavarno on his compliance with the SRA's non-compete agreements.

Because we find there was no procedural unconscionability, the arbitration provisions were not unconscionable and thus are enforceable. (See *Armendariz v. Foundation Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83, 114.)

DISPOSITION

The order is reversed. DePuy Synthes Sales, Inc. is awarded its costs on appeal.

NOT TO BE PUBLISHED.

DHANIDINA, J.

We concur:

LAVIN, Acting P. J. EGERTON, J.